TRIS RATING
A Strategic Partner of S&P Global

CreditNews ข่าวเครดิต

THAI POLYCONS PLC

No. 198/2022
28 October 2022

CORPORATES

Company Rating: BBB-
Outlook: Stable

Last Review Date: 29/10/21

Company Rating History:

Date	Rating	Outlook/Alert
29/10/21	BBB-	Stable
09/10/18	BBB	Stable

Contacts:

Rapeepol Mahapant
rapeepol@trisrating.com

Supasith Tiensuksai, CFA
supasith@trisrating.com

Parat Mahuttano
parat@trisrating.com

Monthian Chantarklam
monthian@trisrating.com

WWW.TRISRATING.COM

RATIONALE

TRIS Rating affirms the company rating on Thai Polycons PLC (TPOLY) at “BBB-”, with a “stable” outlook. The rating reflects the reliability of the cash flow generation from the company’s power business, which essentially countervails the impact from the cyclical nature of its construction business. Conversely, the rating is weighed down by the feedstock supply risk of the power plants and volatile prices, as well as the increasingly competitive renewable power industry. The rating is also pressured by the company’s mediocre competitive position with very thin margins in the construction business.

KEY RATING CONSIDERATIONS

Reliability of cash flows from power business

TPOLY’s rating mainly stems from the reliability of the cash flows from its power business, which currently represents more than 90% of its earnings before interest, taxes, depreciation, and amortization (EBITDA). The power business is carried out by its core and profit-making subsidiary, TPC Power Holding PLC (TPCH). Currently, TPCH owns and operates ten biomass power plants and one waste-to-energy (WTE) power plant, with a combined contracted capacity of 106.5 megawatts (MW).

The reliable cash flows from the power business are derived from the company’s multi-year power purchase agreements (PPAs) with credible state-owned producers and distributors of electricity. The earnings from the power business are crucial in our assessment of TPOLY’s credit profile, helping counteract the volatile earnings of the construction business.

Susceptibility to feedstock risk

TPOLY’s power business is highly susceptible to feedstock supply risk. The biomass power plants use woodchip, rice husk, coconut shells, and other fast-growing plants to produce electricity. The availability of feedstock relies on several factors, such as seasonality, the use of biomass in other industries, and the number of biomass power plants.

To ensure the availability of feedstock, TPCH has secured long-term supply agreements with local suppliers. That said, contract enforcement remains a significant risk. Moreover, earnings of power plants are also exposed to the volatile prices of feedstock. Biomass fuel prices can swing wildly while feedstock varies in terms of humidity and calorific value.

As for WTE, different types of waste provide different calorific value, while contaminants can affect operational stability. The performance of TPCH’s first WTE power project remains to be seen as it just started operations in late 2021.

Weakened performance of power business

TPOLY’s power business experienced a significant drop in operating performance during the first half of 2022 as some of its power plants generated lower-than-expected outputs. The newly added power generating units underperformed and needed longer periods of fine-tuning, while its two existing plants endured serious machinery breakdowns. In the first half of 2022, the average capacity factor plunged to about 70%, significantly below previous records of about 90%. Looking ahead, we expect the company to address the technical problems of some of its power plants and gradually return overall plant efficiency to normal.

Heightening competition in power business

We see the growth opportunities of renewable power in Thailand as the government is bent on increasing the proportion of renewable energy. We expect the opening of a new quota for purchasing electricity from renewable energy sources. However, we view competition in the domestic power market as having mounted in recent years. Meanwhile, the high excess reserve of capacity could deter the development of new power projects.

TPCH's most recent biomass power plants receive lower tariff rates, due to highly competitive bidding. Therefore, TPCH will need to double down on production cost control. Investment in additional green-field or brown-field projects could offer inferior returns due to low tariff rates or high acquisition costs. This should continue to weigh on TPCH's return on investment over the long term. Looking forward, we expect TPCH to shift towards developing WTE projects, considering the more attractive tariff rates than biomass power projects. TPCH may also expand internationally for further growth opportunities. However, domestic projects should remain as the company's core assets and performance.

Mediocre competitiveness in construction business

With respect to the construction business, we view TPOLY as having mediocre competitive position, given its business scale and track record. Most of the company's construction work is worth below THB1 billion per contract, resulting in a small revenue base of about THB2 billion per annum. TPOLY also engages in a narrow scope of construction work, focusing on the construction of buildings, such as hospitals, universities, hotels, and shopping malls.

The government's continued efforts to improve the country's infrastructure leads to a positive view on the domestic construction industry over the medium term. In our view, public sector construction appears to have a brighter outlook than private sector construction. However, delays in the bidding and awarding of public projects, plus severe competition, constrain contractors' profit margins, creating barriers to entry, particularly for small contractors. As a result, TPOLY is leaning towards private projects over the next three years.

Expansion into new ventures

TPOLY endeavors to diversify its businesses. The company recently acquired a 20% stake in Y.S.S.P. Aggregate Co., Ltd. (Y.S.S.P.), which holds long-term concessions to sell raw water for industrial use in the Rayong area. TPOLY also expanded to the automatic car parking and air purification businesses. However, we do not expect a significant revenue contribution from the new businesses as they are at an early stage of operations.

Thin construction margins

Making up about half of total revenue, the construction business will remain important to TPOLY's overall performance. This business has performed weakly due to the recent surge in raw material prices and escalating expenses related to the Coronavirus Disease 2019 (COVID-19) lockdowns. The upward revision on project costs plunged the gross margin of the construction business into a negative 9.1% in 2021 and a negative 3.5% in the first half of 2022.

We expect TPOLY to strive to improve the gross margin of its construction business as planned. The company has recently moved towards higher-margin mechanical and electrical engineering (M&E) works and centralized the procurement of raw materials to enhance bargaining power with suppliers. However, the low-margin works in its construction backlog, worth about 3.5 billion as of June 2022, will likely keep the gross margin of the construction business below 6%. Inclusive of the lucrative power business, TPOLY's gross margin should range between 11%-17% during 2022-2024.

Expectation of improved performances

The rating affirmation embeds our expectation of TPOLY improving its operating performances in both power and construction businesses. In our base case, we project TPOLY's total operating revenue to be THB5.2-THB6.3 billion per year in 2022-2024. Revenue from the construction business, plus the new ventures, should range between THB2.3-THB2.7 billion per annum, while revenue from the power business should range between THB2.8-THB3.5 billion per annum. We assume TPOLY will secure new construction contracts worth about THB1 billion in 2022 and THB2 billion per year during 2023-2024, with no new housing projects to be launched in coming years.

We expect the profit margins of the construction and power businesses to recover, boosting its EBITDA to about THB1.1 billion per year during 2023-2024, up from THB0.6 billion in 2022. Funds from operations (FFO) should increase to THB0.8 billion per year during 2023-2024 from THB0.3 billion in 2022. Its EBITDA margin should be about 11% in 2022, before improving to 17% during 2023-2024.

Financial leverage expected to decline

TPCH guarantees the debts of the incorporated joint ventures (JVs) in proportion to its stakes in the JVs. In assessing the financial profile and performance of TPOLY, we include the assets, liabilities, and respective financial performances of the JVs in TPOLY's consolidated accounts, in proportion to the ownership stake of TPCH in each venture.

TPOLY's financial profile weakened recently, with a surge in its debt to EBITDA ratio to 13.6 times in the first half of 2022. However, we expect the earnings recovery to lower the ratio to about 6 times during 2023-2024. The FFO to debt ratio is projected to improve to 12% during 2023-2024, from about 5% in 2022. The debt to capitalization ratio should range between 60%-65% over the forecast period. We assume annual capital spending of THB0.3-THB0.9 billion over the next three years. TPOLY should also manage its working capital for the construction business efficiently to avoid a rise in financial leverage.

Debt structure

In assessing the level of priority debt in TPOLY's borrowings, we exclude the debt incurred by the JVs which is guaranteed by TPCH. As such, TPOLY's consolidated debt was THB6.3 billion as of June 2022, of which THB5.5 billion was considered priority debt, comprising TPOLY's secured debt and all borrowings incurred by its operating subsidiaries. The priority debt to total debt ratio was 87%, suggesting that the company's unsecured creditors are significantly disadvantaged to its priority debt holders with respect to claims against the company's assets.

Manageable liquidity

TPOLY had short- and long-term loans coming due in the next 12 months of about THB1.5 billion in total as of June 2022. We expect TPOLY to be able to rollover its short-term loans, which are mainly utilized for construction activities. Moreover, the company had undrawn credit facilities, plus cash and marketable securities, of THB1.2 billion. FFO is forecast at THB530 million. Hence, total sources of liquidity are assessed as being about THB1.7 billion, sufficient to cover all the debt due over the next 12 months.

The company's debenture obligations require the company to maintain an interest-bearing debt to equity ratio below 2.5 times. The ratio stood at 1.7 times as of June 2022. Moreover, the company's subsidiaries, including TPCH and its subsidiaries, as well as JVs, are required to maintain a debt service coverage ratio above the varying thresholds of 1.1 times and 1.2 times and a debt-to-equity ratio below the varying thresholds of 1.2 times, 1.5 times, and 2.5 times. We expect each company to meet the financial covenants set forth under its respective loans for the next 12-18 months.

BASE-CASE ASSUMPTIONS

- Aggregate contracted capacity of TPCH's operating power plants to increase to about 112 MW in the next three years.
- Average capacity factor of operating power plants to range between 75%-90% during 2022-2024.
- New contracts for construction work to be worth about THB1 billion in 2022 and THB2 billion per year during 2023-2024.
- Gross margin of construction business to be 0% in 2022, 4% in 2023, and 5.8% in 2024.
- EBITDA margin to be about 11% in 2022 and 17% during 2023-2024.
- Total capital spending to range between THB0.3-THB0.9 billion per annum.

RATING OUTLOOK

The "stable" outlook reflects our expectation that the power business will continue to be the core cash flow generator for TPOLY. This is in addition to the performance of both construction and power businesses gradually recovering. As such, TPOLY's financial leverage and cash generation against debt obligations should be at levels in line with our forecast.

RATING SENSITIVITIES

A downward revision to the rating could develop if the performance of the construction business and/or the power business falls significantly short of our estimates, or if the capital structure deteriorates materially due to aggressive debt-funded investments. The prospect of a rating upgrade is limited but could occur if TPOLY's cash generation against debt obligations improves significantly.

COMPANY OVERVIEW

Established in 1988, TPOLY is a construction contractor providing engineering and construction (E&C) services to the public and private sectors. The company focuses on constructing buildings and civil works. The company was listed on the Market for Alternative Investment (MAI) in 2009 before switching to the Stock Exchange of Thailand (SET) in 2010. TPOLY expanded into the residential property and the power businesses in 2010. It spun off the power business to TPCH, its subsidiary, in 2012. The Chanpalangsri family remained the major shareholder, holding an approximately 44% interest in TPOLY, as of August 2022.

The construction business made up about half of TPOLY's total revenue. However, the power business accounted for the majority of TPOLY's earnings. EBITDA of the power business made up more than 90% of TPOLY's EBITDA during the past three years. As of September 2022, TPOLY's power portfolio had an aggregate contracted capacity of 112.2 MW, across 12 biomass power projects (104.2 MW), and one WTE project (8 MW). Eleven of its power plants are currently operating (106.5 MW).

KEY OPERATING PERFORMANCE

Table 1: Revenue Breakdown

Unit: %

Segment	2018	2019	2020	2021	Jan-Jun 2022
Construction	49	55	55	43	46
Property	3	1	1	0	0
Power	46	43	45	57	53
Trading	1	0	0	0	0
Total	**100**	**100**	**100**	**100**	**100**
Total revenue (mil. THB)	**3,367**	**3,798**	**3,974**	**4,344**	**2,326**

Source: TPOLY

Table 2: Power Project Portfolio (as of Sep 2022)

Company/Country	Held by TPCH (%)	Status	Installed Capacity (MW)	Contracted Capacity (MW)	Tariff
Biomass Projects					
CRB	73	Operating	9.5	9.2	FiT
MWE	85	Operating	9.0	8.0	FiT
MGP	46	Operating	9.5	8.0	FiT
TSG	65	Operating	9.5	9.2	FiT
PGP	60	Operating	9.9	9.2	FiT
SGP	51	Operating	9.9	9.2	FiT
PTG	95	Operating	23.0	21.0	Adder
TPCH1	99	Operating	9.9	9.2	FiT
TPCH2	99	Operating	9.9	9.2	FiT
TPCH5	99	Operating	6.3	6.3	FiT
PBM	59	Constructing	3.0	2.9	FiT
PBB	59	Constructing	3.0	2.9	FiT
Sub total - Biomass			**112.4**	**104.2**	
Waste Projects					
SP	50	Operating	9.5	8.0	FiT
Sub total - Waste			**9.5**	**8.0**	
Grand total			**121.9**	**112.2**	

Source: TPCH

CRB = Chang Raek Bio Power
MGP = Mahachai Green Power
PGP = Phathalung Green Power
PTG = Pattani Green
TPCH2 = TPCH Power 2
PBM = Pracharat Biomass Mae Lan
SP = Siam Power
MWE = Maewong Energy
TSG = Thungsung Green
SGP = Satun Green Power
TPCH1 = TPCH Power 1
TPCH5 = TPCH Power 5
PBB = Pracharat Biomass Bannang Sata

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS*

Unit: Mil. THB

	Jan-Jun 2022	-----------Year Ended 31 December -------- 2021	2020	2019	2018
Total operating revenues	2,401	4,391	3,906	3,827	3,564
Earnings before interest and taxes (EBIT)	59	95	448	606	690
Earnings before interest, taxes, depreciation, and amortization (EBITDA)	248	481	704	797	863
Funds from operations (FFO)	98	275	581	667	750
Adjusted interest expense	142	194	123	102	108
Capital expenditures	137	504	1,428	1,704	731
Total assets	12,399	11,997	10,903	9,981	7,496
Adjusted debt	6,755	5,676	4,673	3,834	2,097
Adjusted equity	3,624	3,803	4,448	4,197	3,785
Adjusted Ratios					
EBITDA margin (%)	10.32	10.96	18.03	20.83	24.21
Pretax return on permanent capital (%)	1.09 **	0.97	5.05	8.26	11.39
EBITDA interest coverage (times)	1.74	2.48	5.73	7.85	7.97
Debt to EBITDA (times)	13.63 **	11.80	6.64	4.81	2.43
FFO to debt (%)	3.37 **	4.85	12.44	17.41	35.76
Debt to capitalization (%)	65.08	59.88	51.24	47.74	35.65

Note: The figures include assets, liabilities, and the respective financial performances of MGP and SP, in proportion to the ownership stake in these JVs.

* *Consolidated financial statements*

** *Adjusted with trailing 12 months*

RELATED CRITERIA

- Group Rating Methodology, 7 September 2022
- Corporate Rating Methodology, 15 July 2022
- Key Financial Ratios and Adjustments for Corporate Issuers, 11 January 2022
- Issue Rating Criteria, 15 June 2021

Thai Polycons PLC (TPOLY)

Company Rating:	BBB-
Rating Outlook:	Stable

TRIS Rating Co., Ltd.
Silom Complex Building, 24th Floor, 191 Silom Road, Bangkok 10500, Thailand Tel: +66 2 098 3000